Jul 17, 2006
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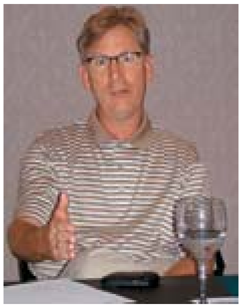
Hotel & Motel Management



Gary Stougaard, executive v.p. and chief investment officer, Sunstone Hotel Investors says revenue growth will follow economy.

NEW YORK—If a rising tide does lift all boats, the lodging industry's armada is cruising at full speed, and can take on just about any rogue swell it faces.

And, according to members of the Lodging Industry Investment Council, the industry has one big weapon that it hasn't used to its fullest advantage to fend off any notion of an economic downturn.

"We look at things particularly from the real-rate side, and in most markets, on a real-rate basis, there's a lot of room to run," said Henry Vickers, principal with AEW Capital Management. "There's likely to be more real-rate expansion in this cycle."

Real rate is the result of the average daily rate increasing more than the increase in consumer price index inflation.

Participants in two LIIC roundtables held in conjunction with the 28th annual New York University International Hospitality Industry Investment Conference in June said they believe aggressively pursuing ADR increases is one of the fundamentals for successful performance during the next few years.

"Just to get back to the same absolute rate, or noninflation-adjusted rate, as we were at in 2000, really isn't a win because we've had six or seven years of inflation in between," said Gary Stougaard, executive v.p. and chief investment officer for Sunstone Hotel Investors (62 hotels comprising more than 18,200 guestrooms in its portfolio). "In major markets where there's limited supply, and as long as the economy keeps percolating along, we're going to see high single-digit, low double-digit revenue growth [from real-rate growth]."

LIIC's mission

"Overall, the hotels in most markets have fully recovered on the revenue side, if not surpassed where they were in the high point of the cycle last time," said Sean Hennessey, c.e.o. of Lodging Investment Advisors.

Bill Blackham, president and c.e.o. of Eagle Hospitality Properties Trust (12 upper-upscale full-service hotels comprising 3,200 guestrooms in its portfolio), said adopting an aggressive ADR policy takes different approaches.

"Some of that will be simply demand driven, but some of it will be premium rates captured through increased guest experience," he said. "Not by amenity creep, but by providing a better-quality guest experience and hence, how well the market is performing."

C.A. Anderson, executive v.p., acquisitions & development for Interstate Hotels & Resorts (a management company that operates 282 hotels comprising nearly 64,000 guestrooms), said achieving the highest top-line revenue is important as more profits become eroded during the flow-through process.

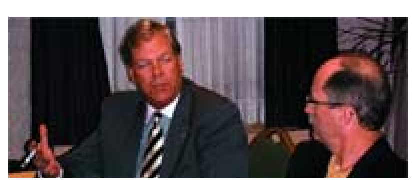
Henry Vickers, principal with AEW Capital Management, said there is likely to be more real-rate expansion in this cycle.

"Everyone is driving us on flow-through—whether it's the opportunity funds that are looking for 60 percent flow-through on that additional dollar or it's more traditional owners who are happy to take 45 [percent] or 50 [percent], it's all coming through on cost control," he said. "It's about working with the brands on amenity creep, or managing the things we typically haven't, such as trying to recoup the losses in the telephone department. We're not bumping salaries like we used to, perhaps, they're performance-based now so they get to share in the yield that's generated by the team that's driving the profitability."

The midscale-without-food-and-beverage segment is proving to be a stalwart rate generator during good times and bad times, said Mark Lomanno, president of Smith Travel Research.

Lomanno said STR is conservatively estimating overall rate growth at 6.7 percent this year, but the midscale-without-food-and-beverage sector should outpace that.

"On an annualized basis, that segment is the rate [increase] leader," Lomanno said. "This didn't happen like this in any prior cycle. Usually the high-end properties, luxury, upper-upscale and so forth, are the rate leaders and everybody else kind of travels along behind.



"In this cycle, while rate growth there has been very strong, the rate growth in midscale-without-food-and-beverage category especially is very strong."

He said what makes it more unique is that only 30 percent of the rooms in the segment are in the top 25 market statistical areas, which have a propensity to be able to drive rates faster.

Kirk Kinsell, senior v.p. and chief development officer for InterContinental Hotels Group, said the midscale-without-food-and-beverage segment finally is getting its due. Included in IHG's global portfolio of about 3,600 hotels comprising about 540,000 guestrooms, includes the Holiday Inn Express brand, (1,435+ hotels comprising 117,000+ guestrooms) which competes in the midscale-without-food-and-beverage segment.

"One of the things that is important that we're hearing here is this is the first time that someone at Smith Travel has something nice to say about midscale-with-food-and-beverage," said Kinsell, tongue-in-cheek. "It's been a category that has been pooh-poohed for [a long time]."

Kinsell pointed to double-digit revenue-per-available-room growth from Express properties as a signal that the segment is performing at its peak.

Blackham cautioned that the industry can't get caught in a wave of over-excitement.

"You can make a case that we're still in a sluggish and somewhat lethargic economy, and yet, the hospitality business is approaching record profits," he said. "There are a lot of storm clouds on the horizon as it relates to the general economic cycle, and yet the hospitality business continues to hum along.

"We're able to capture a higher rate, although expense creep is taking away some of that in terms of profitability."

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